IN THE

Supreme Court of the United States

OCTOBER TERM, 1958

No. 29

WILLIAM B. CAMMARANO and LOUISE CAMMARANO, His Wife, *Petitioners,*

v.

UNITED STATES OF AMERICA.

On Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

BRIEF FOR THE PETITIONERS

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INDEX

AUTHORITIES

CASES: Page

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OPINIONS BELOW

The oral opinion of the district court (R. 27-30) is not reported. The opinion of the court of appeals (R. 134-139) is reported at 246 F. 2d 751.

JURISDICTION

The judgment of the court of appeals (R. 139) was entered on July 8, 1957. A timely petition for rehearing and for rehearing *en banc* was denied on October

15, 1957 (R. 140). The petition for certiorari was filed on January 9, 1958, and granted on March 3, 1958 (R. 140). The jurisdiction of this Court rests on 28 U. S. C. § 1254(1).

QUESTIONS PRESENTED

1. Whether, where taxpayers make payments to a publicity program designed to defeat an initiative measure submitted to the voters at large, which measure would have destroyed the taxpayers' business, the Commissioner of Internal Revenue may by regulation disallow such payments as business expenses in the face of a statute permitting deductions of "All ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business."

2. Whether a regulation forbidding deduction of expenditures for "the promotion or defeat of legislation" may properly be construed and applied to bar deduction of expenditures made to defeat an initiative measure submitted to the people at large.

3. Whether, where the uncontroverted evidence, as well as facts within judicial notice, show that an initiative measure aimed at closing all privately-owned establishments selling beer and wine at retail would destroy 90% of all wholesale businesses in those commodities, it was open to the district court to find (or for the court of appeals to base its additional affirmance on the ground) that it was not shown that the forced closing of retail stores would affect wholesale business.

STATUTES, REGULATION, AND STATE CONSTITUTIONAL PROVISION INVOLVED

The statutes, regulation, and state constitutional provision involved are set forth in the Appendix, *infra*, pp. 67-70.

STATEMENT

The present proceeding is an action brought to recover income taxes for the year 1948 that the petitioners had paid under protest.

Petitioners, husband and wife (Fdg. 1, R. 44), owned a one-fourth interest in a partnership carrying on wholesale distribution of beer under the trade name of "Cammarano Brothers" in Tacoma, Washington (Fdg. 4, R. 45).

At the Washington State general election held on November 2, 1948, an initiative measure was submitted to the people in accordance with Amendment 7 to the Constitution of the State of Washington (*infra*, pp. 69-70). That Initiative to the Legislature, No. 13, would have placed the retail sale of wine and beer exclusively in state-owned and operated stores.

The ballot title of Initiative No. 13 provided:

> "An Act prohibiting the retail sale of beer and wine by any person other than the State of Washington, repealing all provisions of existing law pertaining to licensing of retail sale of beer and wine, revoking existing licenses and providing penalties." (Fdg. 6, R. 45) [1]

[1] The ballot title, under Washington law, was formulated by the Attorney General of the State. Wash. Rev. Code, §§ 29.79.040, 29.79.060. The full text of the initiative measure appears at R. 93-96. Under Washington law, arguments for and against an

The measure had previously, in 1947, been submitted to the state legislature, which did not act upon it (Fdg. 7, R. 45-46). Subsequently the Initiative was submitted to the people in 1948, in which year the legislature was not in session (Pretrial order, ¶ 7, R. 22-23).

Petitioners were members of the Washington Beer Wholesalers Association, Inc. (Fdg. 5, R. 45), a non-profit trade association exempt from federal income tax (Fdg. 10, R. 47; Pretrial order, ¶ 6, R. 22; Pl. Ex. 4, R. 149-150).[2] This Association in December 1947 established the Washington Beer Wholesalers Association, Inc., Trust Fund, to help finance an extensive statewide publicity program, on the part of wholesale and retail beer and wine dealers, which urged the defeat of Initiative No. 13 (Fdgs. 5-6, R. 45).[3]

Payments to the Trust Fund were made by the Association's members on the basis of the volume of business of each wholesaler (Fdg. 8, R. 46). During 1948, the partnership of Cammarano Brothers paid $3,545.15 to the Trust Fund, of which petitioners' proportionate share was $886.29 (Fdg. 5, R. 46).

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initiative measure are, after formulation by its proponents and opponents, distributed by the Secretary of State at public expense. See Wash. Rev. Code, §§ 29.79.340 to 29.79.430. The text of the arguments for and against Initiative No. 13 are set forth at R. 96-101.

[2] The Association's Articles of Incorporation appear at R. 141-148.

[3] In 1947, while the measure had been pending in the state legislature, an officer of the Beer Wholesalers Association had kept close track of its progress, personally contacted many of the legislators, and urged its defeat (Fdg. 7, R. 45-46). Any expenditures made in that connection by the Beer Wholesalers Association are not in issue in the present proceeding.

The Trust Fund was expended in furtherance of the publicity program against Initiative No. 13 (R. 114-116), which was carried out by various types of advertising—newspaper, radio, direct mail, billboards, streetcar cards (R. 115-116)—none of which had reference to the wares or members of the Association as such (Fdg. 8, R. 46).[4]

Initiative No. 13 was defeated (Fdg. 9, R. 46).

In filing their joint federal income tax return for the year 1948, petitioners deducted as a business expense under Sec. 23(a)(1)(A) of the Internal Revenue Code of 1939 as amended (*infra*, page 67), their proportionate part of the payment made by the partnership to the Trust Fund in the campaign against Initiative No. 13 (Cmplt., ¶ V, R. 4; Exh. A to Complt., R. 11-12; Ans. ¶¶ 5, 7, R. 13-14, 14-15).

The Commissioner disallowed the expenditures in question on the ground that Treas. Reg. 111, Sec. 29.23(o)-1 (*infra*, pp. 67-69) barred deductions of "Sums of money expended for lobbying purposes, the promotion or defeat of legislation, the exploitation of propaganda" (Cmplt., ¶ VI at R. 5-6; Ans., ¶ 6, R. 14; Pretrial order, ¶ 5, R. 22), and assessed an additional tax against petitioners, of which the sum of $153.98 was attributable to such disallowance (Pretrial order, ¶ 5, at R. 22).

After payment under protest of the additional tax assessed, and failure of the Commissioner to act upon

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[4] Examples of the advertising campaign against Initiative No. 13 in daily and weekly newspapers were contained in Pl. Ex. 7 (R. 151-182). That exhibit was not included in the printed record in the court of appeals, but was designated by the Government for printing here after certiorari was granted.

petitioners' timely claim for refund, they brought the present action for the recovery of the tax so paid under protest (Fdg. 3, R. 44).

On the day of the trial, the Government filed a trial memorandum with the district court which stated, *inter alia* (R. 18), "Concededly, Initiative 13 would have affected a portion of plaintiffs' business, and perhaps would have put them out of business entirely." Government counsel in his opening statement sought to qualify or withdraw this concession (R. 73-74).

The only oral testimony on the point was offered by Adwen, Secretary of the Washington Beer Wholesalers Association (R. 75), who testified (R. 76-77):

> "A. Initiative 13 primarily would have in the opinion of the industry—I think I can safely say industry—would have made it necessary to distribute beer and wine through state liquor stores which would have automatically put the taverns and grocery stores handling beer and wine out of business. At the same time it would undoubtedly have put at least 90 per cent of the beer wholesalers out of business. I don't say a 100 per cent for this reason. It would still probably be necessary for some of the breweries to have representatives to call upon the Liquor Board to sell their merchandise and their wares, but at least 90 per cent of them would have had nothing to do so they would have gone completely out of business."

Under the terms of Initiative No. 13 (R. 93-96), the State of Washington was granted a monopoly of the retail sale of beer; all laws pertaining to the licensing of the retail sale of beer were repealed; and all existing retail licenses for the sale of beer were revoked.

Notwithstanding all of the foregoing, the trial court found as a fact that (Fdg. 9, R. 46):

> "There was testimony to the effect that the Initiative, if passed, would have affected the wholesale business of Cammarano Brothers. However, the way in which the measure, aimed as it was at retail sales of wine and beer, would have affected the wholesale distribution of beer was not made clear."

The district judge, both in his oral opinion rendered at the close of the trial (R. 27-30) and in his formal conclusions of law filed four months later (R. 37-48), held for the Government on the ground that the regulation relied upon was valid and that there was no distinction between efforts to influence legislation that were addressed to the legislature and efforts directly addressed to the people in connection with an initiative measure.

He specifically held, however, that the expenditures made by petitioners were perfectly proper, saying orally (R. 29):

> "* * * This is not to indicate that there is anything evil or corrupt about spending money for these purposes. Quite the contrary. The expenditure of money to enlighten and inform the public with respect of initiative measures is a perfectly proper and laudable activity. When the general public are called upon to enact or refuse to enact legislation, the more information they are given and the more widespread it is distributed the better. Certainly neither this taxpayer nor the Washington Brewers Institute nor the brewing industry are in any manner to be criticized for having spent the money to defeat the legislation by fair publicity. They had a

right to do that and propriety of expenditures therefor is not in question. * * *"

Later he formally found as a fact (Fdg. 11, R. 47) that:

"* * * There was nothing wrong or evil or corrupt about spending money for this purpose. Expenditures to enlighten and inform the public with respect to initiative measures are perfectly proper and laudable."

After judgment for the defendant (R. 49-50), petitioners appealed to the court below (R. 51). The court held (R. 134-138) that the regulation disallowing the expenditure was proper and applied to situations where the proposed legislation was before the people, as well as where the legislation was only before a legislature. The court rested its affirmance on the additional ground (R. 138-139) that, in view of Finding 9 (*supra*, page 7) petitioners failed to establish "that the passage of the initiative would have impaired its business as a beer distributor." A timely petition for rehearing was denied (R. 140), after which this Court granted certiorari (R. 140).

SUMMARY OF ARGUMENT

I. A. Sums expended by a taxpayer to preserve his business or occupation from destruction are, as a matter of law, deductible as ordinary and necessary business expenses. *Commissioner* v. *Heininger*, 320 U. S. 467. On that principle, the deduction claimed in the present case should have been allowed, for petitioners' expenses here were incurred to save their existing business from destruction and not merely in an attempt to create a new business for the future.

B. Where, however, allowance of a deduction would frustrate sharply defined state or national policy, the expenditure is not regarded as "necessary". Penalties paid because of violation of state laws are an example. *Tank Truck Rentals* v. *Commissioner,* 356 U. S. 30; *Hoover Express Co.* v. *United States,* 356 U. S. 38. But the policies frustrated must be national or state policies evidenced by some governmental declaration, and therefore an optician who shared his profits with doctors in order to remain in business was held entitled to deduct his payments, however much they may have been unethical so far as the doctors were concerned. *Lilly* v. *Commissioner,* 343 U. S. 90. Lobbying expenses are not deductible, *Textile Mills Corp.* v. *Commissioner,* 314 U. S. 326, because lobbying —the use of personal influence on individual legislators, personal solicitation, the spreading of insidious influences through legislative halls—offends against well recognized public policy.

C. But while lobbying is condemned, open, honest, non-lobbying efforts directed at obtaining the enactment of legislation by overt advocacy are not. This Court's decisions recognize the validity of such latter efforts even in situations where the compensation payable is contingent on the enactment of the legislation. *E.g., Nutt* v. *Knut,* 200 U. S. 12; *McGowan* v. *Parish,* 237 U. S. 285; *Winton* v. *Amos,* 255 U. S. 373. Thus it is plain that what was done here, which did not involve lobbying in its narrow and invidious sense, was not within the condemnation of *Textile Mills;* the latter decision dealt only with lobbying—"that family of contracts to which the law has given no sanction"—and it has always been thus narrowly construed by this Court.

D. Insofar as the regulation now in question goes beyond lobbying as such, and denies deductions for "Sums of money expended for * * * the * * * defeat of legislation," it goes beyond the scope of *Textile Mills*; it disregards the well settled distinction between lobbying, which is condemned, and legitimate legislative activity, which is not; and it ignores *Commissioner* v. *Heininger,* 320 U. S. 467, which holds that expenditures to save an existing business from destruction are "ordinary and necessary" as a matter of law. There is no warrant in the statute or in any decisions here for the purported blanket rule that no expenditures in connection with legislation are ever deductible, regardless of circumstances. Here, as in *Bingham's Trust* v. *Commissioner,* 325 U. S. 365, the Commissioner has by fiat carved an exception out of the statute; here, as in *Bingham's Trust*, the regulation is unauthorized.

II. In any event, a regulation denying deductibility to expenditures made for the defeat of "legislation" cannot validly be construed to cover legislation enacted, not by a legislature, but directly by the people themselves in the exercise of their underlying residual sovereignty. The notion that "legislation is legislation", espoused below, overlooks completely a significant phase of American political development that had its origin in popular distrust of legislative bodies, and that sought a solution in restoration of the people's sovereignty through direct legislation by the people in initiative and referendum. The holding below, that activities directed at legislation pending in legislative halls are identical with activities directed at legislation pending before the electorate at large, would preclude the attainment of the very objectives of the initiative, a device adopted to protect the people from the frailties of their legislators, and from the

lobbying pressures to which the latter were subjected. The distinction between lobbying, with all its sordid connotations of insidious influences, and the attempts here involved, "to saturate the thinking of the community," is clear-cut, and has received recognition here. *United States* v. *Rumely,* 345 U. S. 41; *United States* v. *Harriss,* 347 U. S. 612. Indeed, any attempt to equate the two would raise serious constitutional questions here, since to deny an exemption to taxpayers who engage in certain forms of speech is in effect to penalize them for such speech. *Speiser* v. *Randall,* 357 U. S. 513, 518.

The Tax Court, in allowing deductions for expenses incurred in furthering a constitutional amendment that a lawyer taxpayer considered helpful in improving his practice, recognized the distinction between arguments directed at a legislature and those addressed to the entire electorate. *Luther Ely Smith,* 3 T. C. 696. There is no sound distinction between that case and this one; neither the constitutional amendment there nor the initiative here required action by the legislature. Both were equally direct legislation enacted by the people in the exercise of their underlying sovereignty. For fourteen years the Commissioner acquiesced in *Luther Ely Smith,* only to withdraw his acquiescence after certiorari was granted in the present case. His new, *post motam litem* position is that sums expended in any attempt to enact or defeat legislation, including a constitution which is fundamental law, are not deductible regardless of the effects of such legislation on the taxpayer's business, is without support in authority, runs counter to the statute, and has only the doubtful merit of novelty.

III. A. The reenactment doctrine does not sustain the regulation in its application to the facts of the

present case. To begin with, that doctrine is subject to serious qualifications: It is unreliable, an auxiliary tool at best, and cannot alter statutory provisions that are clear and explicit when related to the facts disclosed. Moreover, Congress cannot be expected to make an affirmative move whenever a lower court indulges in an erroneous interpretation.

B. The regulation denying deductions for legitimate legislative activities has never been passed on in any situation where the legislation being opposed would necessarily have destroyed the taxpayer's business. Accordingly, it has never been reenacted in that context.

Moreover, Section 23(a) of the Code deals with trade or business expenses, while the regulation now in question is headed and indexed under Sec. 23(o), "Charitable and other contributions." One subsection deals with business expenses, the other with deductible contributions by any taxpayer whether in business or not. Unlike the regulation involved in *Textile Mills,* which had a long history, the present regulation dates only from 1938. Surely if the conscientious Congressman facing the bill that became the Internal Revenue Code of 1939 had sought to ascertain the meaning of "ordinary and necessary" business expenses in draft Section 23(a)(1), he would never have looked to a regulation entitled "Contributions or gifts to individuals" to find that meaning. Nor would it ever have occurred to him that expenditures by a businessman to defeat, without resort to lobbying, legislation that would have destroyed his existing business were not deductible as ordinary and necessary business expenses, by reason of the fact that contributions by taxpayers whether in business or not were not

deductible when made to organizations substantially engaged in opposing legislation.

C. It is even more clear that there has been no reenactment of the regulation denying deductions for legislative expenses in its application to legislation enacted directly by the people without intervention of a legislature. For the Commissioner publicly acquiesced over a period of 14 years in *Luther Ely Smith*, 3 T. C. 696, which held the contrary. Thus there is no scope for the reenactment doctrine in the present case—except insofar as that doctrine, in the face of such an acquiescence, supports petitioners.

IV. Petitioners sufficiently proved that passage of the proposed initiative measure, which would have closed all retail stores for the sale of beer, would have impaired their wholesale business to the point of probable destruction.

The terms of the initiative, together with the uncontradicted oral testimony that 90% of all beer wholesalers would have been put out of business, established that its passage would substantially have destroyed petitioners' business. A wholesaler sells to retailers, and when there are no retailers to sell to—which is what the initiative would have meant—he is out of business. The alternative holding of the courts below that petitioners did not sustain their burden of proof on the issue of destruction of business is a consequence of thinking in terms of words rather than of commercial relationship. Facts within judicial notice, even apart from the evidence in the record, establish the connection between the initiative's closing of retail stores and the consequent destruction of petitioners' wholesale business. The alternative holding below is also deficient on narrower and more technical grounds;

the finding on which it rests is "clearly erroneous" under Rule 52(b), F.R.Civ.P., and the doctrine of judicial admissions precludes withdrawal of the Government's formal concession prior to trial that the initiative measure would have put petitioners out of business.

Nor is there substance in the Government's new contention that petitioners' proof is deficient in not showing that they would have been within the 90% of the beer wholesalers put out of business. Mathematical certainty is not required; a genuine threat is sufficient to establish that expenditures made to avert the destruction so threatened are "ordinary and necessary" in the context of the statute. *Commissioner* v. *Heininger*, 320 U. S. 467, 472. Nothing turns on mere percentages here; a 90 per cent threat is enough.

ARGUMENT

The present petitioners, individual taxpayers, seek to establish a deduction in respect of money spent to defeat an initiative measure that would have destroyed their existing business. Both courts below held that this could not be done in the face of a regulation stating that "Sums of money expended for lobbying purposes [and] the promotion or defeat of legislation" were not deductible.

It is petitioners' first position that, while expenditures for lobbying purposes—the exercise of personal influence and solicitation on individual legislators—are properly disallowed as deductions on grounds essentially of public policy, there is no warrant for similarly denying deductions for legitimate and open efforts directed against legislation which would have

destroyed an existing business, and that the regulation thus applied runs counter to the statute.

It is petitioners' alternative position that, whatever may be the case in respect of legislation enacted by a legislature, the regulation in question cannot in any event apply to legislation enacted by the people through the instrumentality of the initiative, and that to do so would raise a serious constitutional issue.

I. Expenses Incurred in Openly Opposing, Without Lobbying, Legislation That Would Have Destroyed the Taxpayers' Business, Do Not Run Counter to Sharply Defined State or National Policies, and Are Therefore Deductible as Ordinary and Necessary Business Expenses; and a Regulation Purporting to Disallow Such Expenditures Is Accordingly Invalid Because Contrary to the Statute.

A. Sums spent in an endeavor to protect a taxpayer's business from destruction are deductible as ordinary and necessary business expenses.

Ever since 1918, see *Kornhauser* v. *United States*, 276 U. S. 145, the American taxpayer has been permitted to deduct from net income "All the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business."[5] For the taxable year in question in the present case, this provision appeared in Sec. 23(a)(1)(A), I.R.C. 1939 (*infra*, p. 67).[6] There have been literally thousands of decisions turning on what constitutes "ordi-

[5] Sec. 214(a)(1) of the Revenue Acts of 1918, 1921, 1924, and 1926; Sec. 23(a) of the Revenue Acts of 1928, 1932, 1934, and 1936; Sec. 23(a)(1) of the Revenue Act of 1938. Earlier provisions were the same in substance though slightly different in language. Sec. II(B)[2] of the Revenue Act of 1913; Sec. 5(a) (First) of the Revenue Act of 1916.

[6] The corresponding provision of I. R. C. 1954 is § 162(a).

nary and necessary expenses." Today even more than twenty-five years ago (*Welch* v. *Helvering,* 290 U. S. 111, 116), "To attempt to harmonize them would be a futile task." This much, however, is now clear: Sums expended by the taxpayer to preserve his business or occupation from destruction are deductible.

The leading case is *Commissioner* v. *Heininger,* 320 U. S. 467, where a mail order dentist, threatened with being put out of business by a Post Office fraud order, incurred legal expenses in defending the proceedings. Although he was ultimately unsuccessful in his defense, see *Heininger* v. *Farley,* 105 F. 2d 79 (D. C. Cir.), certiorari denied, 308 U. S. 587, he was permitted to deduct the legal fees paid. This Court said (320 U. S. at 471, 472):

> "It is plain that respondent's legal expenses were both 'ordinary and necessary' if those words be given their commonly accepted meaning. For respondent to employ a lawyer to defend his business from threatened destruction was 'normal;' it was the response ordinarily to be expected. * * * Since the record contains no suggestion that the defense was in bad faith or that the attorney's fees were unreasonable, the expenses incurred in defending the business can also be assumed appropriate and helpful, and therefore 'necessary.' * * * To say that this course of conduct and the expenses which it involved were extraordinary and unnecessary would be to ignore the ways of conduct and the forms of speech prevailing in the business world."

The *Heininger* result had been foreshadowed by Mr. Justice Cardozo's discussion in *Welch* v. *Helvering,* 290 U. S. 111, 114:

> "Ordinary in this context does not mean that the payments must be habitual or normal in the sense

that the same taxpayer will have to make them often. A lawsuit affecting the safety of a business may happen once in a lifetime. The counsel fees may be so heavy that repetition is unlikely. None the less, the expense is an ordinary one because we know from experience that payments for such a purpose, whether the amount is large or small, are the common and accepted means of defense against attack. Cf. *Kornhauser* v. *United States,* 276 U. S. 145. The situation is unique in the life of the individual affected, but not in the life of the group, the community, of which he is a part."

And so, in a variety of situations, sums expended by a taxpayer to preserve his business or occupation from destruction have been held deductible. Thus, an officer facing a court-martial and the consequent risk of dismissal from the service may deduct counsel fees incurred in defending against the charges, since, of course, his business is that of being an officer, and the court-martial would determine whether he should lose that status and its income concomitants. *Lindsay C. Howard,* 16 T. C. 157, affirmed on another issue, 202 F. 2d 28 (C. A. 9). A motion picture scenario writer, summoned to appear before a Congressional committee and facing possible blacklisting by the industry, may deduct the sums paid counsel for representing him with a view to preventing his loss of livelihood. *Waldo Salt,* 18 T. C. 182. A public entertainer may deduct counsel fees incident to the prosecution of an action for libel brought solely for the protection of his business income. *Paul Draper,* 26 T. C. 201. And expenditures made to protect a taxpayer's business reputation are similarly deductible. *Laurence M. Marks,* 27 T. C. 464. It is only when such expenditures are related to personal as distinguished from business

reputation that they are non-deductible under the statute. *Joseph Lewis,* 27 T. C. 158, affirmed *sub nom. Lewis* v. *Commissioner of Internal Revenue,* 253 F. 2d 821 (C. A. 2).

On the foregoing principle, the deduction claimed in the present case should have been allowed. As Mr. Justice (then Judge) Minton said in the *Heininger* case below (*Heininger* v. *Commissioner of Internal Revenue,* 133 F. 2d 567, 570 (C. A. 7)), later quoted with approval by this Court in *Lilly* v. *Commissioner,* 343 U. S. 90. 94, note 4,

> "If the deduction in the case at bar was not an ordinary and necessary expense to the 'carrying on' of the business, we are unable to understand the English language. Without this expense, there would have been no business. Without the business, there would have been no income. Without the income there would have been no tax. To say that this expense is not ordinary and necessary is to say that that which gives life is not ordinary and necessary."

A very similar question was recently passed upon by the House of Lords. *Morgan* v. *Tate & Lyle Ld.,* [1955] A. C. 21, affirming [1953] Ch. 601. There a corporation threatened with nationalization expended corporate funds in campaigning against such a course on the part of Parliament. It was held that such sums were deductible within Rule 3(a), a regulation having the force of law because a part of the Schedule to the Act in question, as (p. 36) "disbursements or expenses * * * wholly and exclusively laid out or expended for the purposes of the trade." Lord Morton of Henryton said (p. 39 of [1955] A. C.):

> "Can it properly be held that money spent to prevent seizure by the State of the company's assets,

> including the goodwill of the business carried on by the company, is money 'wholly and exclusively laid out or expended for the purposes of the trade' within the meaning of rule 3(*a*)? * * *
>
> "My Lords, apart from authority I should have no hesitation in answering the question just posed in the affirmative. Looking simply at the words of the rule I would ask: 'If money so spent is not spent for the purposes of the company's trade, for what purpose is it spent?' If the assets are seized, the company can no longer carry on the trade which has been carried on by the use of these assets. Thus the money is spent to preserve the very existence of the company's trade."[7]

It is significant that in the present case petitioners' expenses were incurred to save their existing business from destruction and not merely in an attempt to create a new business in the future. The latter may for present purposes be assumed to be non-deductible by analogy to the holding in *McDonald* v. *Commissioner,* 323 U. S. 57, 60—"his campaign contributions were not expenses incurred in being a judge but in trying to be a judge for the next ten years." It is on that basis that most instances of expenses incurred in direct appeals to the electorate in the endeavor to legal-

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[7] Where however a pamphlet is circulated with purposes not solely of advancing the company's trade, the expenses incurred are non-deductible. *Boarland* v. *Kramat Pulai Ld.,* [1953] 1 W. L. R. 1332 (Ch. D.). An earlier Privy Council case, which disallowed expenses incurred by brewers in persuading the public to vote against prohibition in New Zealand, is distinguishable, because there the statute (p. 149) disallowed expenses "not exclusively incurred in the production of the assessable income derived from that source," and hence is not regarded as authority in England for English income tax legislation, which has a different statutory standard for deductible business expenses. *Ward & Co.* v. *Commissioner of Taxes,* [1923] A. C. 145, 149-150; see *Morgan* v. *Tate & Lyle Ld.,* [1955] A. C. at 43, 49-50, 63.

ize a future business presently illegal have been disallowed. *E.g., Mrs. William P. Kyne,* 35 B. T. A. 202 (horse racing); *cf. Mays* v. *Bowers,* 201 F. 2d 401 (C. A. 4) (to be elected a city councilman); *cf.* also *Old Mission P. Cement Co.* v. *Commissioner of Int. Rev.,* 69 F. 2d 676 (C. A. 9), affirmed on other issues, 293 U. S. 289 (effects of referendum measure on business held too remote). But petitioners here did not appeal to the voters to gain office prospectively or to be permitted to engage in a business then unlawful; they made the expenditures in an ultimately successful effort to preserve from certain destruction an existing business then and now entirely lawful.

There is accordingly no need at this juncture to reexamine *McDonald* v. *Commissioner,* 323 U. S. 57, which, since no opinion of the Court was rendered therein, cannot be considered as authoritative.[8] For present purposes petitioners are content to rest on the clear distinction between their situation—threatened destruction of an existing business—and that of *McDonald*—the attempt to embark on a new business.

B. Where allowance of a deduction would frustrate sharply defined state or national policy, the expenditure is not regarded as "necessary", and accordingly sums expended for lobbying purposes, an activity that contravenes public policy because of its sinister tendencies, are not deductible.

Certain limitations on deductibility foreshadowed by the *Heininger* case, 320 U. S. at 473—"that tax deduction consequences might not frustrate sharply defined national or state policies proscribing particular types of conduct"—were clarified at the Term just

[8] "* * * the lack of an agreement by a majority of the Court on the principles of law involved prevents it from being an authoritative determination for other cases." *United States* v. *Pink,* 315 U. S. 203, 216; *Hertz* v. *Woodman,* 218 U. S. 205, 212-214.

past. Thus, penalties paid by truck owners and their employees for violating penal laws of a state are non-deductible, *Tank Truck Rentals* v. *Commissioner*, 356 U. S. 30, even if inadvertent. *Hoover Express Co.* v. *United States*, 356 U. S. 38. In the same category of non-deductibility are payments of hush money (*Samuel Towers*, 24 T. C. 199, 244-247), payments for solicitations of insurance forbidden by state insurance laws (*Boyle, Flagg & Seaman, Inc.*, 25 T. C. 43), and payments of bribes by way of "protection" (*Cohen* v. *Commissioner of Internal Revenue*, 176 F. 2d 394, 400-401 (G. A. Comeaux) (C. A. 10)).

On the other hand, expenses such as rent and salaries that are plainly deductible in respect of a lawful enterprise do not lose their deductibility because incurred in the conduct of a business that is clearly unlawful. *Commissioner* v. *Sullivan*, 356 U. S. 27. The thrust of "sharply defined national or state policies" does not, in the absence of clear expression of Congressional intent, operate to make an illegal enterprise pay taxes on a gross receipts basis.

Moreover, "The policies frustrated must be national or state policies evidenced by some governmental declaration of them." *Lilly* v. *Commissioner*, 343 U. S. 90, 97. Consequently, as the Court held in that case, the Commissioner could not disallow on grounds of public policy deductions of kickback payments made by opticians to physicians in the regular course of their optical enterprise. The payments in question were unethical in the eyes of many doctors, but still they were ordinary and necessary business expenses within the Internal Revenue Code in the context of the opticians' business. This Court accordingly reversed successive holdings by the Tax Court and the Court of Appeals that had denied the deductions on

the basis that they violated public policy. The Court said (p. 93):

> "The payments likewise were 'necessary' in the generally accepted meaning of that word. It was through making such payments that petitioners had been able to establish their business. Discontinuance of the payments would have meant, in 1943 or 1944, either the resumption of the sale of glasses by the doctors or the doctors' reference of their patients to competing opticians who shared profits with them."

Thus the Court in *Lilly* reaffirmed the holding in *Heininger* that expenditures incurred for preserving an existing business are, as a matter of law, "ordinary and necessary" within the meaning of Sec. 23(a)(1)(A), I. R. C. 1939.

There still remains an area not yet clarified by decisions of this Court. As we have pointed out, *Heininger* allowed the deduction of legal expenses incurred in unsuccessfully seeking to set aside a postal fraud order that put the taxpayer out of business, and did so in the face of contentions by the Commissioner (Pet. Br., No. 63, Oct. T. 1943, at 20) that "To allow the deduction would be to allow compensation for the costs which law enforcement has caused the one who has transgressed," and that (*id.*, 21) "We know of no instance heretofore where expenditures incurred as the result of unsuccessfully resisting disciplinary measures instituted by the sovereign have been permitted by the courts to be deducted as ordinary and necessary business expenses."

In *Heininger*, the "disciplinary measures instituted by the sovereign" took the form of a fraud order supported by substantial evidence. *Heininger* v. *Farley*, 105 F. 2d 79, *supra*. Thereafter, Congress passed the

Federal Denture Act of 1942, now 18 U. S. C. § 1821, that prohibited the interstate transportation of dentures under stated conditions even in the absence of fraud. See *United States* v. *Johnson*, 323 U. S. 273. Suppose that, at the present time, the "disciplinary measures instituted by the sovereign" against Dr. Heininger or other dentists similarly situated took the form of a prosecution under 18 U. S. C. § 1821; would the legal fees incurred in defending such a prosecution be deductible? The state of the present cases seems to be that such fees can be deducted only if the prosecution fails, not if it succeeds. See *Commissioner* v. *Heininger*, 320 U. S. 467, 473, note 8; see also cases collected in 104 A. L. R. 680, 683-686; 20 A. L. R. 2d 600, 612-617. The Tax Court has recently refused deduction for legal expenses incurred in unsuccessfully resisting disbarment proceedings following conviction for crime. *Thomas A. Joseph*, 26 T. C. 562. Since the defendant who is acquitted is allowed his deduction, it is hardly open to urge that a similarly allowed deduction for the convicted client subsidizes obduracy (cf. *Jerry Rossman Corporation* v. *Commissioner of Int. Rev.*, 175 F. 2d 711, 713 (C. A. 2)), and we should suppose that the public policy of the Sixth and Fourteenth Amendments, provisions that so clearly recognize the constitutional basis of the effective assistance of counsel (*Powell* v. *Alabama*, 287 U. S. 45; *Johnson* v. *Zerbst*, 304 U. S. 458; *Gibbs* v. *Burke*, 337 U. S. 773), would militate against penalizing a taxpayer who availed himself of the protection that those Amendments afford him.

We do not need to formulate an answer now, but the speculations just canvassed are far from irrelevant here, in view of the Government's contentions

that petitioners have not proved to a mathematical certainty that the initiative measure in his case would have put them out of business. See Point IV, at pp. 63-65, *infra*.

We return to those areas where the law is certain. If a taxpayer engages in lobbying to advance his business, he cannot deduct his lobbying expenses. *Textile Mills Corp.* v. *Commissioner*, 314 U. S. 326. There (p. 336) "A publicist was retained to arrange for speeches, news items, and editorial comment. Two legal experts were retained to prepare propaganda concerning international relations, treaty rights and the policy of this nation as respects alien property in time of war." Moreover, "F. W. Mondell, an attorney and a former member of Congress, was employed in connection with the preparation and making of proposals and suggestions to members of Congress, 'the aim of which was to promote the speedy enactment of the desired legislation.'" 38 B. T. A. at 625; 117 F. 2d at 63.[9] As a former member of the House, Mr. Mondell had the privilege of its floor, subject only to his being "not interested in any claim or directly in any bill pending before Congress" (Rule XXXIII(1), H. R. Doc. 661, 68th Cong., 2d sess.; *id.*, H. R. Doc. 781, 69th Cong., 2d sess.; *id.*, H. R. Doc. 629, 70th Cong., 2d sess.) The quoted language was not construed until 1945 to cover former members of the House "in the employ of an organization that is interested in legislation before the Congress" (H. R. Doc. 489, 84th Cong., 2d sess., p. 489). Moreover, Mr.

[9] No question was raised either before the Board of Tax Appeals on the Third Circuit as to the deductibility of sums subsequently paid Mr. Mondell for legal services in connection with specific claims. See 38 B. T. A. at 626, 627; 117 F. 2d at 64.

Mondell had been majority floor leader in the 66th and 69th Congresses. *Biographical Directory of the American Congress,* 1774-1949, H. R. Doc. 607, 81st Cong., 2d sess., pp. 1575-1576. Thus the Government is plainly in error in suggesting (Br. Op. 8) that no direct dealings with individual legislators were involved in the *Textile Mills* case.

This Court pointed out (p. 337) that "The ban against deductions of amounts spent for 'lobbying' as 'ordinary and necessary' expenses of a corporation derived from a Treasury Decision in 1915. T. D. 2137, 17 Treas. Dec. Int. Rev. pp. 48, 57, 58."

Further (pp. 338-339)—

> "Contracts to spread such insidious influences through legislative halls have long been condemned. *Trist* v. *Child,* 21 Wall 441; *Hazelton* v. *Sheckels,* 202 U. S. 71. Whether the precise arrangement here in question would violate the rule of those cases is not material. The point is that the general policy indicated by those cases need not be disregarded by the rule-making authority in its segregation of non-deductible expenses. There is no reason why, in the absence of clear Congressional action to the contrary, the rule-making authority cannot employ that general policy in drawing a line between legitimate business expenses and those arising from that family of contracts to which the law has given no sanction. The exclusion of the latter from 'ordinary and necessary' expenses certainly does no violence to the statutory language. The general policy being clear it is not for us to say that the line was too strictly drawn."

Petitioners do not question *Textile Mills* in any way. Their position under Point I of this brief is that, as the findings (R. 47; *cf.* R. 29) show, they did

not engage in lobbying in the invidious sense; that *Textile Mills* applies, and has been understood as applying, only to lobbying; and that it does not apply to legitimate non-lobbying efforts in connection with legislation, which, as this Court has frequently recognized, do not belong to "that family of contracts to which the law has given no sanction."

C. Decisions of this Court recognize a clear distinction between open, honest, non-lobbying efforts directed at legislation, such as were involved in the present case, and the character of activities long characterized as lobbying.

This Court has repeatedly and consistently recognized a clear line of distinction between the insidious practice of lobbying and the wholly proper activity of obtaining the enactment of legislation by open advocacy.

The essence of lobbying lies in personal solicitation and in the exercise of personal influence, acts that are furthered by secrecy, and by the circumstance that the principal on whose behalf the influence is exerted is so often an undisclosed one. The evil tendencies reflected in the *Textile Mills* record—an astute publicity man spreading propaganda impossible to trace to its source; a lawyer of acknowledged reputation writing articles on abstract questions of international morality without disclosing that he was doing so on behalf of a client; an ex-Congressman (and ex-majority leader) availing himself of his floor privileges to buttonhole and to cajole legislators, including former colleagues —those were activities familiar to the lobbyists of a much earlier age. See *Marshall* v. *Baltimore & O. R. Co.*, 16 How. 314, and see particularly the outline of

the techniques used, pp. 316-319, which, we might add, are hardly less cynical or less effective than anything devised in the more than 110 years that have passed since. In condemning as illegal the contract for lobbying services involved in that case, this Court emphasized that its primary vice lay in the secrecy surrounding the process of solicitation. See 16 How. at 335:

> "* * * But where persons act as counsel or agents, or in any representative capacity, it is due to those before whom they plead or solicit, that they should honestly appear in their true characters, so that their arguments and representations, openly and candidly made, may receive their just weight and consideration. A hired advocate or agent, assuming to act in a different character, is practicing deceit on the Legislature. * * * Any attempts to deceive persons intrusted with the high function of legislation, by secret combinations, or to create or bring into operation undue influence of any kind, have all the injurious effects of a direct fraud on the public. * * *
>
> "Influences secretly urged under false and covert pretences must necessarily operate deleteriously on legislative action, whether it be employed to obtain the passage of private or public acts. Bribes, in the shape of high contingent compensation, must necessarily lead to the use of improper means, and the exercise of undue influence. * * *"

The doctrine of the *Marshall* case, where this Court first had occasion to deal with the evil propensities of lobbying that offended against public policy, was followed in *Trist* v. *Child*, 21 Wall. 441, 451:

> "The agreement in the present case was for the sale of influence and exertions of the lobby agent to bring about the passage of a law for the pay-

> ment of a private claim, without reference to its merits, by means which, if not corrupt, were illegitimate and, considered in connection with the pecuniary interest of the agent at stake, contrary to the plainest principles of public policy."

Again, a lobbying contract was condemned in *Hazelton* v. *Sheckels,* 202 U. S. 71, 79:

> "The objection to them rests in their tendency, not in what was done in the particular case. * * * In its inception, the offer, however intended, necessarily invited and tended to induce improper solicitation, and it intensified the inducement by the contingency of the reward."

But contracts to procure legislation by properly and openly presenting the facts to the appropriate committees or legislative bodies stand on a very different footing. Such agreements have been uniformly upheld by this Court over a long period. *Spalding* v. *Mason,* 161 U. S. 375 (recovery on contract for part of fees earned for prosecuting claims and urging passage of necessary legislation; arrangement apparently contingent); *Nutt* v. *Knut,* 200 U. S. 12 (recovery for services in getting claim legislatively allowed where no lobbying was involved, but where payment was contingent on passage); *McGowan* v. *Parish,* 237 U. S. 285 (same); *Winton* v. *Amos,* 255 U. S. 373 (same); *Steele* v. *Drummond,* 275 U. S. 199 (contract by property owner to secure a franchise from a municipal legislative body held valid).

The distinction between the contract for lobbying purposes that contravenes public policy, and the contract to endeavor to secure legislation by legitimate means was early set forth. See *Trist* v. *Child,* 21 Wall. 441, 450:

"* * * an agreement express or implied for purely professional services is valid. Within this category are included; drafting the petition to set forth the claim, attending to the taking of testimony, collecting facts, preparing arguments, and submitting them orally or in writing, to a committee or other proper authority, and other services of like character. All these things are intended to reach only the reason of those sought to be influenced. They rest on the same principle of ethics or professional services rendered in a court of justice, and are no more exceptionable. But such services are separated by a broad line of demarcation from personal solicitations, and the other means and appliances which the correspondence shows were resorted to in this case. There is no reason to believe that they involved anything corrupt or different from what is usually practiced by all paid lobbyists in the prosecution of their business."

In *Nutt* v. *Knut,* 200 U. S. 12, recovery turned on whether the efforts of the lawyer in obtaining legislative relief for the client involved lobbying. This Court disposed of that matter in these terms (200 U. S. at 21-22):

"Much was said in argument as to the nature of the services rendered by the plaintiff—the charge being that his services were of the kind called *lobby* services for which, consistently with public policy and public morals, no recovery could be had in any court. *Trist* v. *Child,* 21 Wall. 441; *McMullen* v. *Hoffman,* 174 U. S. 639. We have seen that the state court of original jurisdiction was of opinion the suit was for lobbying services, and on that ground denied all relief. But the Supreme Court of Mississippi held that the record did not establish such a case, and we accept that view of the evidence in the cause."

Again, in *Winton* v. *Amos*, 255 U. S. 373, the same distinction was emphasized in a case allowing recovery for services rendered in obtaining legislation to benefit particular Indians. This Court said (pp. 392-393):

> "The claim of Winton, Owen, and associates, is based wholly upon services rendered—nothing being asked because of expenses incurred or moneys disbursed. According to the findings the services rendered were in the nature of professional services before Congress and its committees, individual Representatives and Senators, the Dawes Commission, etc., intended to establish the right of the Mississippi Choctaws to participation in the material benefits of citizenship in the Choctaw Nation, and to secure such legislation by Congress as might be needed for the practical attainment of the object sought. The findings render it clear that services of this nature, altogether proper in character,—not lobbying, in the odious sense,—were rendered by these claimants under particular employment by many individual Mississippi Choctaws, but with the object, incidentally, of benefitting the Mississippi Choctaws as a class, because only so could the clients of the claimants be benefited. We make no doubt that, for proper professional services rendered, and expenses incurred in promoting legislation that has for its object and effect the rescue of substantial property interests for a class of beneficiaries under a trust of a public nature, it is equitable to impose a charge for reimbursement and compensation upon the interests of those beneficiaries who receive the benefit, the same as if a like result had been reached through successful litigation in the courts. In either case there is the same curious analogy to the salvage services of the maritime law; and while it may be more difficult to weigh the effect of a service rendered in promoting legislation, and to estimate its value, than in a case of successful litigation, we think

the principle of *Internal Improv. Fund* v. *Greenough* and *Central R. & Bkg. Co.* v. *Pettus* applies in the one case as in the other."

It is particularly to be noted that recovery under the contracts involved in *Nutt* v. *Knut,* 200 U. S. 12; *McGowan* v. *Parish,* 237 U. S. 285; and *Winton* v. *Amos,* 255 U. S. 373, was frankly and clearly contingent upon passage of the contemplated legislation, and that the same appears to have been the fact in *Spalding* v. *Mason,* 161 U. S. 375. Thus there is nothing in the fact of contingency that condemns the arrangement. The contract is legal and consistent with public policy whether contingent or otherwise, just so long as the services to be rendered in connection with obtaining enactment of the legislation in question are open and professional. It is only when the contract looks to lobbying—the exercise of personal influence, the use of personal solicitation—that the arrangement stands condemned.

In *Steele* v. *Drummond,* 275 U. S. 199, 206, the Court cited the lobbying cases—"The claims there considered were under contracts requiring or contemplating the obtaining of legislative or executive action as a matter of favor by means of personal influence, solicitation and the like, or by other improper means."

"But," the Court continued, "this case is different. Drummond was not employed by Steele or by the railroad company to secure the passage of the ordinances. He was interested as an owner of property. Neither the contract, nor what was done, suggests that the location or construction of the proposed line was not a legitimate enterprise undertaken for the public good, or that anything improper was contemplated as a means to secure the passage of the ordinances. Drummond's object was to obtain the railway service; and, for

that purpose, he expended a large sum. The mere fact that he owned property that might be favorably affected does not tend to discredit him or to make evil his undertaking to obtain the ordinances. His interest in having the railroad extended into St. Andrews gave him the right in every legitimate way to urge the passage of appropriate ordinances. There is nothing that tends to indicate that in the promotion or passage of them there was any departure from the best standards of duty to the public. The contention that Drummond's agreement to secure their passage was contrary to public policy cannot be sustained."

Under the distinctions set forth, it is plain that what was done in the case at bar was open, above-board, legitimate, and in no sense violative of public policy. The district court specifically so found (Fdg. 11, R. 47): "There was nothing wrong or evil or corrupt about spending money for this purpose. Expenditures to enlighten and inform the public with respect to initiative measures are perfectly proper and laudable."

Earlier the district judge had said orally (R. 29):

"* * * This is not to indicate that there is anything evil or corrupt about spending money for these purposes. Quite the contrary. The expenditure of money to enlighten and inform the public with respect of initiative measures is a perfectly proper and laudable activity. When the general public are called upon to enact or refuse to enact legislation, the more information they are given and the more widespread it is distributed the better. Certainly neither this taxpayer nor the Washington Brewers Institute nor the brewing industry are in any manner to be criticized for

having spent the money to defeat the legislation by fair publicity. They had a right to do that and propriety of expenditures therefor is not in question. * * *" [10]

On the facts of this case, as in connection with the contract for a concession considered in *Valdes* v. *Larrinaga,* 233 U. S. 705, 709, 710, there was nothing "that necessarily imports, or even persuasively suggests, any improper intent or dangerous tendency"; "the things done * * * have no sinister smack." In short, no lobbying was involved.

It follows that what was done here was not within the condemnation of *Textile Mills.* For that case dealt solely and exclusively with lobbying, and has always been understood to be limited to situations involving lobbying.

The facts in *Textile Mills* involved, as has been pointed out (pp. 24-25, *supra*), precisely the secrecy and the use of personal influence that were condemned as early as *Marshall* v. *Baltimore & O. R. Co.,* 16 How. 314. And the distinction drawn in the *Textile Mills* opinion, quoted *supra* p. 25, "between legitimate business expenses and those arising from that family of contracts to which the law has given no sanction", must be read against the line of cases just discussed, from *Spalding* v. *Mason,* 161 U. S. 375,

[10] Before the initiative in the present case was submitted to the people, it had previously been submitted to the legislature, at which time an officer of the Beer Wholesalers Association contacted many of the legislators, urging defeat of the proposal. Fdg. 7, R. 45-46. This may well have been lobbying—but no deduction was or is sought in respect to any sums then expended in that connection.

to *Steele* v. *Drummond,* 275 U. S. 199, which show that legitimate, overt, legislative activity related to a business, far from warranting condemnation, constitutes the basis for agreements that the courts will enforce. Plainly, nothing in *Textile Mills* condemns legislative activity free from the taint of lobbying.

Nor does *Textile Mills* rest on the circumstances that the compensation to be paid the taxpayer there was contingent upon passage of the Settlement of War Claims Act. A contract for legal services looking to the enactment of legislation for a client's benefit, where compensation for such services is entirely contingent upon passage of the legislation, is perfectly legal and does not contravene public policy. *Nutt* v. *Knut,* 200 U. S. 12; *McGowan* v. *Parish,* 237 U. S. 285; *Winton* v. *Amos,* 225 U. S. 373; *Spalding* v. *Mason,* 161 U. S. 375 (*semble*). There is accordingly nothing in the discussion in *Textile Mills* that rests on the feature of contingency; the thrust of the opinion is that (314 U. S. at 338) "Contracts to spread * * * insidious influences through legislative halls have long been condemned." And, as we have also said, nothing in *Textile Mills* condemns legislative activity free from the taint of lobbying.

It is thus that *Textile Mills* has always been construed by this Court. In *Commissioner* v. *Heininger,* 320 U. S. 467, 473, it was cited for the proposition that "one who has incurred expenses for certain types of lobbying and political pressure activities with a view to influencing federal legislation has been denied a deduction." Similarly, in *Lilly* v. *Commissioner,* 343 U. S. 90, 95, it was said that in *Textile Mills* "this Court accepted an interpretation of [§23(a)(1)(A)]

by a Treasury Regulation which disallowed the deduction of certain expenses for lobbying purposes." [11]

The result is that *Textile Mills* does not reach the present case, where no lobbying was involved.

D. Insofar as the regulation purports to prohibit deductions for "Sums of money expended for * * * the * * defeat of legislation" in a situation where the legislation would have destroyed the taxpayers' existing business, it is in conflict with the Code which affirmatively permits deduction of "ordinary and necessary business expenses", and is to that extent invalid.

The regulation considered in *Textile Mills,* Art. 262 of Treas. Reg. 74, "Donations by corporations", stated in pertinent part that "Sums of money expended for lobbying purposes, the promotion or defeat of legislation * * * are not deductible from gross income." But, as we have just shown at some length, the *Textile Mills* decision dealt only with "money expended for lobbying purposes", and has always been understood as applying only to lobbying.

The lower courts, however, have misread *Textile Mills,* and have construed it as authority for the much broader proposition that expenditures for "the promotion or defeat of legislation" were similarly condemned by that decision, in every situation, and regardless of circumstances. This was done by the Court below in this case, see R. 136, n. 3, even though

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[11] For what it is worth, the Government in each case similarly limited its characterization of *Textile Mills.* See the Commissioner's Briefs in *Heininger* (Pet. Br., No. 63, Oct. T. 1943, at 16) ("* * * this Court has recently refused to sanction the deductibility, as an ordinary and necessary business expense, of lobbying expenditures to procure legislation") and in *Lilly* (Resp. Br., No. 158, Oct. T. 1951, at 54) ("the lobbying activities involved in the *Textile Mills* case").

the opinion uses the word "lobbying" no less than seven times in characterizing the regulation in question. R. 135, 136, 137, 138. The difference between lobbying and legitimate legislative activities that is expounded in the decisions of this Court cited and discussed above, pp. 28-34, was not even considered by the court below or in any of the decisions which it cited (R. 136, n. 2) or which the Government invoked in opposition to the petition for certiorari (Br. Op. 5-6).[12]

Every lower court that has considered this question has woodenly construed *Textile Mills* to condemn all legislative efforts, and every lower court that has considered this question has been utterly unaware of the rule that open legislative efforts are thoroughly legitimate and that contracts for such efforts, unlike contracts to lobby, are enforceable, have been enforced by this Court, and so are not within "that family of contracts to which the law has given no sanction." *Textile Mills,* 314 U. S. at 339.

A fortiori, where open legislative efforts are directed towards saving an existing legitimate business from destruction, and where no public policy is violated, the principle of *Commissioner* v. *Heininger,* 320 U. S.

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[12] *F. Strauss & Son, Inc., of Ark* v. *Commissioner of Int. Rev.,* 251 F. 2d 724 (C. A. 8), certiorari granted, 356 U. S. 966 (No. 50, this Term); *Revere Racing Association* v. *Scanlon,* 232 F. 2d 816 (C. A. 1); *American Hardware & Eq. Co.* v. *Commissioner,* 202 F. 2d 126 (C. A. 4), certiorari denied, 346 U. S. 814; *Roberts Dairy Co.* v. *Commissioner,* 195 F. 2d 948 (C. A. 8), certiorari denied, 344 U. S. 865; *Sunset Scavenger Co.* v. *Commissioner,* 84 F. 2d 453 (C. A. 9); *Old Mission P. Cement Co.* v. *Commissioner,* 69 F. 2d 2d 676 (C. A. 9), affirmed on other issues, 293 U. S. 289; *Wm. T. Stover Co.,* 27 T. C. 434; *Herbert Davis,* 26 T. C. 49; *McClintock-Trunkey Co.,* 19 T. C. 297, reversed on other grounds, 217 F. 2d 329 (C. A. 9).

467, comes into play. Such expenditures are "ordinary and necessary" within the statute. It follows that the ruling below, and the other decisions of lower courts relied on by the court below and by the Government here, all rest on a misreading of controlling authorities in enunciating a blanket rule that no expenditures in connection with legislation are deductible.

The result is that, as applied to the present case the regulation in question—Section 29.23(o)-1 of Treas. Reg. 111 (*infra*, pp. 67-69)—is necessarily invalid under the familiar principle that the application of any regulation in conflict with the meaning and purpose of a statute is unauthorized and hence without effect. *E.g., Bingham's Trust* v. *Commissioner*, 325 U. S. 365, 377; *Manhattan General Equipment Co.* v. *Commissioner*, 297 U. S. 129, 134-135. We do not consider it necessary to labor that principle or to expound it in detail.

But we think it appropriate to draw attention to *Bingham's Trust* v. *Commissioner*, 325 U. S. 365, just cited, because of its bearing on the problem here. There the claimed deduction arose under § 23(a)(2) of the 1939 Code, which permitted deduction of "ordinary and necessary expenses paid or incurred for the production or collection of income, or for the management, conservation, or maintenance of property held for the production of income." The trustees had incurred legal expenses in the course of unsuccessfully contesting a tax deficiency. A regulation provided that "Expenses incurred * * * for the purpose of resisting a proposed additional assessment of taxes * * * are not deductible expenses." This Court held that

the regulation was in conflict with the meaning and purpose of the statute, and hence unauthorized.

The parallelism between that case and this one is plain. Here, as in *Bingham's Trust,* there is a regulation that purports to disallow a particular kind of what would otherwise be an ordinary and necessary expense, not on any ground of public policy, but by arbitrary fiat. Here, as in *Bingham's Trust,* therefore, the regulation should be struck down, and for the same reason: It is inconsistent with the deduction that Congress has specifically allowed.

II. In Any Event, a Regulation Denying Deductibility to Expenditures Made for the Defeat of "Legislation" Cannot Validly Be Construed to Cover Legislation Enacted, Not By a Legislature, But Directly by the People Themselves in the Exercise of Their Underlying Residual Sovereignty.

Even if the regulation here in question can be held validly to deny the taxpayer a deduction for sums expended in connection with legitimate, openly conducted legislative activity in connection with legislation pending in a legislature—the usual sense of the word "legislation"—there is no warrant for extending it to legislation directly enacted by the people in the exercise of their underlying residual sovereignty, here through the instrumentality of the initiative.

1. The district judge took the view that "legislation is legislation." He said orally (R. 28-29):

> "* * * In other words, the making of laws is legislation whether the laws are made by a sovereign ruler, a city council, county commissioners, a state legislature, Congress, or by the people directly through an initiative or referendum measure.
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> "In applying the regulation there is no rational basis for making a distinction between sums of

money spent for the purpose of influencing the public in their action on an initiative measure and sums spent with the object of influencing members of the legislature with respect to pending legislation. There certainly is not any ground for making that distinction in the language of the Treasury regulation. The regulation flatly says that sums of money expended for the promotion or defeat of legislation are not deductible from gross income. An initiative measure is just as much legislation as an act of a legislature or any other enactment of law."

Later, in a formal conclusion of law, he repeated that view (R. 48):

"* * * Plaintiffs make much of the fact that the instant publicity campaign was aimed at the people generally rather than the legislature, but no such distinction is recognized by the cited cases nor does it commend itself to reason. Certainly publicity can be directed at legislators both directly and indirectly. But more important for purposes of this case, the measure at which the instant campaign was aimed was clearly legislation, albeit subject to enactment by the people generally rather than members of a legislature."

Insofar as the court below failed to discuss the distinction between legislation by a legislature and legislation enacted directly by the people (R. 135-138), it necessarily espoused the same "legislation is legislation" view.

But such a mechanical application of dictionary definitions does more than disregard the evils inherent in lobbying, an activity plainly not practiced here, and the distinction already canvassed between lobbying and legitimate legislative activity. The views taken below are subject to the far more serious criticism that

they overlook completely an important and highly significant phase of American political development, which had its origin in popular distrust of legislative bodies, and which sought a solution in a restoration of the people's sovereignty in the form of direct legislation by the people effectuated through the initiative and referendum. Amendment 7 to the Constitution of the State of Washington (*infra*, pp. 69-70), pursuant to which the initiative here in question took place, was adopted in 1912, when the movement for measures permitting such direct legislation was at its height.

The supporters of the initiative sought to give the people the power to pass laws independently of the legislature, on the view that in a democracy the control of the people over their government should be continuous and direct. One avowed purpose of the initiative was to obviate the secret control of powerful interests over the limited number of legislators, by lobbying and otherwise. These views are set forth in a host of contemporary writings; the listing that follows is representative rather than exhaustive. See, *e.g.*, *The Initiative, Referendum, and Recall* (43 Annals of the American Academy, No. 132);[13] Theodore Roosevelt, *A Charter of Democracy* [Columbus, Ohio, speech, Feb. 21, 1912], Sen. Doc. 348, 62d Cong., 2d sess., pp. 11-12;[14] Eaton, *The Oregon System* (1912);

[13] "Briefly summarized, the functions of the initiative and referendum are: To restore the sovereignty of the people. To educate and develop the people. To secure legislation for the general welfare. To prevent legislation against the general welfare. To eliminate the legislative blackmailer. To make our legislative bodies truly representative." Sen. Bourne of Oregon, *Functions of the Initiative, Referendum, and Recall*, *id.* at 3.

[14] "We hold it a prime duty of the people to free our Government from the control of money in politics. For this purpose we advocate, not as ends in themselves, but as weapons in the hands

Beard and Schultz, *Documents on the State-Wide Initiative, Referendum and Recall* (1912); Barnett, *The Operation of the Initiative, Referendum, and Recall in Oregon* (1915); DeWitt, *The Progressive Movement* (1915) 213-228; *cf. Pacific States Tel. & Tel. Co.* v. *Oregon*, 223 U. S. 118.

To hold, as did both courts below, that activities directed at legislation pending in legislative halls are to be assimilated to activities directed at a measure presented to the electorate at large, under initiative provisions adopted in a conscious, deliberate effort to protect the people from the frailties of their elected representatives, would preclude the attainment of the very objectives of the initiative. For among the principal objectives of the initiative was the desire to obviate the evils of lobbying and of all other influences on legislators by increasing the control of the people at large over the law-making process. Ironically enough, the rulings under review in this case were made on the West Coast, where the initiative first flourished. Indeed, it is fair to say that the initiative and referendum represent the West's unique contribution to American political structure. And to hold, as did both courts below, that sums expended to oppose an initiative measure, which would have destroyed petitioners' business, are not ordinary and necessary business expenses, is to do violence not only to the language of the governing statute, but also to "the ways of conduct and the forms of speech prevailing in the business world." *Commissioner* v. *Heininger*, 320 U. S. 467, 472.

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of the people, all governmental devices which would make the representatives of the people more easily and certainly responsible to the people's will." *Id.*, p. 3.

2. This Court has twice in recent years distinguished between lobbying, with all its sordid connotations of insidious influences, and attempts such as the one here involved, the purpose of which is "to saturate the thinking of the community." *United States* v. *Rumely,* 345 U. S. 41; *United States* v. *Harriss,* 347 U. S. 612.

In the *Rumely* case, the respondent had been convicted of contempt of Congress for refusing to disclose the names of purchasers of certain books. The resolution constituting the Committee before which he declined to answer was in these terms (p. 44):

> "The Committee is authorized and directed to conduct a study and investigation of (1) all lobbying activities intended to influence, encourage, promote, or retard legislation; and (2) all activities of agencies of the Federal Government intended to influence, encourage, promote, or retard legislation." H. Res. 298, 81st Cong., 1st Sess.

Reversal of conviction by the Court of Appeals, 197 F. 2d 166 (D. C. Cir.)[15] was affirmed by this Court on narrow grounds, to avoid a constitutional issue. The Court said (345 U. S. at 47):

> "* * * As a matter of English, the phrase 'lobbying activities' readily lends itself to the construction placed upon it below, namely, 'lobbying in its commonly accepted sense,' that is, 'representa-

[15] The Court of Appeals had said, though without discussing the holdings of this Court on the point (pp. 28-34, *supra*), "In the past a difference between lobbying and 'purely professional services' in acquainting a legislature with the merits or demerits of measures was recognized at the law. * * * It may be that the line between lobbying in its pristine sense and proper professional service is too shadowy to serve as a limiting barrier to the regulatory power of the Congress. We do not have that question here * * *." 197 F. 2d at 175.

tions made directly to the Congress, its members, or its committees,' 90 App. D. C. 382, 391, 197 F. 2d 166, 175, and does not reach what was in Chairman Buchanan's mind, attempts 'to saturate the thinking of the community.' 96 Cong. Rec. 13883. If 'lobbying' was to cover all activities of anyone intending to influence, encourage, promote or retard legislation, why did Congress differentiate between 'lobbying activities' and other 'activities . . . intended to influence'? Had Congress wished to authorize so extensive an investigation of the influences that form public opinion, would it not have used language at least as explicit as it employed in the very resolution in question in authorizing investigation of government agencies? Certainly it does no violence to the phrase 'lobbying activities' to give it a more restricted scope. * * *"

Similarly, in *United States* v. *Harriss,* 347 U. S. 612, sustaining the validity of the Federal Regulation of Lobbying Act, 2 U. S. C. §§ 261-270, the Court adopted a narrow definition of "lobbying" to save the measure. The Court said (347 U. S. at 620-621):

"We now turn to the alleged vagueness of the purposes set forth in § 307(a) and (b).[16] As in *United States* v. *Rumely,* 345 U. S. 41, 47, which involved the interpretation of similar language, we believe this language should be construed to refer only to 'lobbying in its commonly accepted sense'—to direct communication with members of Congress on pending or proposed federal legislation. The legislative history of the Act makes clear that, at the very least, Congress sought disclosure of such direct pressures, exerted by the

[16] "(a) The passage or defeat of any legislation by the Congress of the United States.

"(b) To influence, directly or indirectly, the passage or defeat of any legislation by the Congress of the United States."

> lobbyists themselves or through their hirelings or through an artificially stimulated letter campaign. It is likewise clear that Congress would have intended the Act to operate on this narrower basis, even if a broader application to organizations seeking to propagandize the general public were not permissible." [17]

Whatever may be the scope of Congressional power to require the registration of legitimate representatives, see 347 U. S. at 620, note 10, par. "Third" at 621, it is plain that this Court in *Rumely* and in *Harriss* has recognized the basic and indeed obvious difference between arguments directed at a legislature and arguments directed at the electorate at large. It need hardly be added that any attempt to equate the two would raise serious problems under the First Amendment in respect of the freedom of both speech and press. See *Speiser* v. *Randall*, 357 U. S. 513, 518: "It cannot be gainsaid that a discriminatory denial of a tax exemption for engaging in speech is a limitation on free speech. * * * It is settled that speech can be effectively limited by the exercise of taxing power. *Grosjean* v. *American Press Co.*, 297 U. S. 233. To deny an exemption to claimants who engage in certain forms of speech is in effect to penalize them for such speech. Its deterrent effect is the same as if the State were to fine them for this speech."

The construction of the regulation that petitioners urge would of course avoid even consideration of any constitutional problem.

3. The Government argued (Br. Op. 8) that activity "to saturate the thinking of the community" "is precisely the type of activity which was involved in *Tex-*

[17] Footnotes omitted.

tile Mills", referring to the preparation and dissemination of news items, speeches, editorials, and similar materials that was there involved. But this argument entirely overlooks the vital distinction between this case and that one.

Here the legislation was put before the people themselves for adoption or rejection. The legislators could not pass on it except as they might cast their own votes as individual citizens in the initiative election. In *Textile Mills,* however, passage or rejection of the Settlement of War Claims Act was dependent on the votes of Senators and Representatives, and the activities directed at the general public affected the members of Congress only indirectly. Overwhelming public approval of the Settlement of War Claims Act would not necessarily result in its enactment, nor would overwhelming public disapproval of its terms preclude its passage. Here, however, the public position on Initiative No. 13 would be directly translated into adoption or rejection. Thus the very purpose of the initiative procedure—that the people might directly express their views on pending measures, that representative government might be translated into popular government—would be attained. The Government's argument accordingly echoes the failure of both opinions below to recognize the difference between initiative legislation directly enacted by the people and ordinary legislation enacted by their representatives.[18]

It seems worth while to add, even at the risk of repetition, that appeals to the electorate can scarcely

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[18] We have already, pp. 24-25 *supra*, adverted to the Government's erroneous assertion (Br. Op. 8) that *Textile Mills* did not involve direct dealings with legislators.

be equated with what was condemned in *Textile Mills* (314 U. S. at 338), the effort "to spread * * * insidious influences through legislative halls."

4. The Tax Court has recognized the distinction between arguments directed at a legislature and publicity addressed to the entire electorate.

In *Luther Ely Smith,* 3 T. C. 696, the question concerned the right of the taxpayer, a trial lawyer, to deduct as an ordinary and necessary business expense a contribution made to an organization formed to amend the Constitution of Missouri by providing that candidates for judicial office should be nominated by a Commission. The taxpayer established that his trial practice had suffered under the existing method of selecting judges because his clients had lost confidence in the courts. The contribution was expended for publicity in support of the amendment in the form of speeches, literature, and radio broadcasts. The amendment was adopted, and, being self-operative, became law forthwith.

In allowing the deduction, the Tax Court rested its conclusion on the basis that no lobbying was involved because the people themselves acted. It said (3 T. C. at 702):

> "It should be noted that the institute engaged in no lobbying of any kind before any legislative body. No legislation was needed or involved in its plan. It contemplated an amendment to the constitution, proposed by the initiative of the people, voted upon at a general election, and becoming self-operative thirty days thereafter, without the necessity of any action or approval by either the legislature or the governor."

We submit that there can be no sound distinction between a campaign directed at the voters generally in respect of a constitutional amendment that takes affect without action of the legislature, and an initiative measure that similarly takes effect. Both are equally direct legislation enacted by the people in the exercise of their underlying sovereignty.

Luther Ely Smith was decided a few years after *Textile Mills.* If the Commissioner had regarded the former case as inconsistent with this Court's *Textile Mills* ruling, it would have been his duty to take an appeal or, at the very least, to have noted his non-acquiescence. In fact, he acquiesced in *Luther Ely Smith,* see 1944 Cum. Bull. 26, and in the Petition for Certiorari we added (Pet. 10), "and his acquiescence has never been withdrawn." That statement was accurate when it was made. Later, however, after the Petition for Certiorari herein was granted, and some fourteen years after the original acquiescence, the Commissioner withdrew it. Rev. Rul. 58-255, *Int. Rev. Bull.,* No. 1958-21, May 26, 1958, pp. 9, 16-17.[19]

Of course this long-delayed change of position has "the usual infirmity of *post litem motam,* self-serving declarations." *United States* v. *Rumely,* 345 U. S. 41, 48. Of genuine weight it has none; and, far from persuading that *Luther Ely Smith* is wrong, this almost comical about-face fourteen years after the event lends strong support to petitioners' view that *Luther Ely Smith* and the decision now under review are inconsistent and cannot stand together. But what is perhaps more significant is that the Commissioner's

[19] On May 26, 1958, the day of issue, this Court also granted certiorari in the *F. Strauss & Son* case, 356 U. S. 966 (now No. 56, this Term.)

belated revelation as to the scope of the regulation is demonstrably unsound.

5. Here is the operative portion of the Commissioner's present position (*Int. Rev. Bull.*, May 26, 1958, p. 17):

> "It has long been the position of the Internal Revenue Service that amounts expended in furtherance of an attempt to promote or defeat legislation, either before a legislature or before the general electorate, are not deductible, for Federal income tax purposes, as ordinary and necessary business expenses within the meaning of section 162 of the Internal Revenue Code of 1954 or corresponding provisions of the 1939 Code. This position has been sustained in *Textile Mills Securities Corporation* v. *Commissioner*, 314 U. S. 326 (1941), C. B. 1941-2, 200; *Sunset Scavenger Co., Inc.* v. *Commissioner*, 84 F. 2d 453 (9th Cir. 1936); *Revere Racing Association* v. *Scanlon*, 232 F. 2d. 816 (1st Cir. 1956); *Commarano* v. *U. S.*, 246 F. 2d 751 (9th Cir. 1957), cert. granted March 3, 1958; and *F. Strauss & Son, Inc.* v *Commissioner*, 251 F. 2d. 724 (8th Cir. 1958).
>
> "Inasmuch as a constitution is a general or fundamental law, an attempt to influence the adoption or rejection by the general electorate of a constitutional amendment is basically an attempt to promote or defeat legislation. Accordingly, expenditures to promote or defeat a constitutional amendment are not deductible as ordinary and necessary business expenses within the meaning of section 162 of the Code."

Passing the point that two of the cases cited are now here and that the foregoing solemn assertion of "It has long been the position", etc., conveniently overlooks that for fourteen years it was the Commissioner's view that a constitutional amendment was not

legislation within the regulation, the basic infirmity of the foregoing categorical, generalized rule now announced is two-fold.

First, it ignores the distinction, fully discussed above, pp. 28-34, between legitimate legislative activity and "that family of contracts to which the law has given no sanction."

Second, it ignores the fact that only improper contracts dealing with matters pending in a legislature—not contracts dealing with matters pending before the voters—have ever been condemned. Here is the rule from the *Restatement of the Law of Contracts:*

> "§ 559. Bargain to Influence Legislation.
>
> "(1) A bargain to influence or to attempt to influence *a legislative body or members thereof,* otherwise than by presenting facts and arguments to show that the desired action is of public advantage, is illegal; and if a method is provided by law for presenting such facts and arguments, a bargain that involves presenting them in any other way is illegal.
>
> "(2) A bargain to conceal the identity of a person on whose behalf arguments to influence legislation are made, is illegal."

We have added the italics to emphasize the lack of foundation for the Commissioner's current views. Those views are accordingly entirely novel. But since this case involves taxes rather than patents, the Government can obtain no advantage from the Commissioner's undoubted priority of invention.

6. It must not be overlooked that, under *Heininger, Lilly, Tank Truck Rentals,* and *Sullivan,* the only basis for denying a deduction for what would be ordinary and necessary business expenses in the light of

"the ways of conduct and the forms of speech prevailing in the business world" would be that the tax deduction consequences would "frustrate sharply defined national or state policies proscribing particular types of conduct." *Heininger* at 472, 473.

Just what national or state policies are frustrated when the people amend their fundamental law, or when, under initiative provisions, they vote on a legislative measure? And just what state or national policies are frustrated when a taxpayer expends sums in opposition to or in support of proposed constitutional amendments or initiative measures that would directly affect his business? To ask these questions is to underscore the capriciously arbitrary nature of the Commissioner's newly formulated expression of supposed public policy.

True, it is the Commissioner's duty to protect the revenue. But it is not part of his duty, and it is certainly not within his competence, to reject the most fundamental aspects of representative government in order to collect a few tax dollars. Here he appears willing—nay, eager—to sell the birthright of democracy that is his in common with his fellow-citizens in order to avoid having to refund $153.98 (R. 10, 15, 21).

In the context of the statute, which permits deduction from gross income of "All the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business;" in the context of the facts, which show petitioners incurring expenses in order to defeat an initiative measure which would have destroyed their existing business; and in the context of the political structure of the State of Washington, which provided as well for

arguments for and against to be addressed to the electorate, it is plain that petitioners' expenditures were legitimate business expenditures whose deduction cannot be denied by administrative fiat.

For, insofar as the present litigation is concerned, the vice of the Commissioner's incursion into political science is that, in the process, he has given his regulation an interpretation that brings it into conflict with the statute.

III. The Reenactment Doctrine Does Not Serve to Sustain the Regulation in Its Application to the Facts of the Present Case.

The court below (R. 138) and the Government in opposing review here (Br. Op. 7) argued that there has been Congressional reenactment of the regulation that is in question in this case. But this "usual last resort" (*Buck* v. *Bell*, 274 U. S. 200, 208) of the tax gatherer will not survive examination.

A. The reenactment doctrine, in all but the clearest cases, is subject to serious qualifications.

To begin with, as this Court has frequently recognized, the doctrine of reenactment is a weak and unreliable reed on which to rest statutory interpretation. "Reenactment—particularly without the slightest affirmative indication that Congress ever had the * * * decision before it—is an unreliable indicium at least. *Helvering* v. *Wilshire Oil Co.*, 308 U. S. 90, 100, 101; *Koshland* v. *Helvering*, 298 U. S. 441, 447." *Commissioner* v. *Glenshaw Glass Co.*, 348 U. S. 426, 431. "But the doctrine of legislative acquiescence is at least only an auxiliary tool for use in interpreting ambiguous statutory provisions. See *Helvering* v. *Reynolds*, 313 U. S. 428, 432. Here the language and the purpose of Congress seem clear to us." *Jones* v. *Liberty Glass*

Co., 332 U. S. 524, 533-534. "Long-continued practice and the approval of administrative authorities may be persuasive in the interpretation of doubtful provisions of a statute, but cannot alter provisions that are clear and explicit when related to the facts disclosed." *Louisville & N. R. Co.* v. *United States*, 282 U. S. 740, 759.

Next, the fact that a few decisions have intervened does not and cannot mean that Congress has by reenactment of the statute approved the decisions. "We do not expect Congress to make an affirmative move every time a lower court indulges in an erroneous interpretation. In short, the original legislative language speaks louder than such judicial action." *Jones* v. *Liberty Glass Co.*, 332 U. S 524, 534. Or, as Judge Learned Hand once expressed the matter, "To suppose that Congress must particularly correct each mistaken construction under penalty of incorporating it into the fabric of the statute appears to us unwarranted; our fiscal legislation is detailed and specific enough already." *F. W. Woolworth Co.* v. *United States*, 91 F. 2d 973, 976 (C. A. 2), certiorari denied, 302 U. S. 768.

Finally, and this is vital in the present connection, "the rule that re-enactment of a statute after it has been construed by officers charged with its enforcement impliedly adopts the construction applies only when the construction is not plainly erroneous and to cases presenting the precise conditions passed on prior to the re-enactment." *United States* v. *Missouri P. R. Co.*, 278 U. S. 269, 279-280.

The Government's reenactment arguments must now be considered in the light of the foregoing principles.

B. The regulation denying deductions for legitimate legislative activities has never been passed on in a situation where the legislation being opposed would have destroyed the taxpayer's business, and hence was never reenacted in that context.

None of the cases relied on by the court below and by the Government here under the reenactment doctrine involved the situation of expenditures opposing legislation which would have destroyed a taxpayer's existing business. Here they are (R. 138; Br. Op. 7): (1) *Textile Mills Corp.* v. *Commissioner,* 314 U. S. 326; (2) *Sunset Scavenger Co.* v. *Commissioner,* 84 F. 2d 453 (C. A. 9); (3) *Roberts Dairy Co.* v. *Commissioner;* 195 F. 2d 948 (C. A. 8), certiorari denied, 344 U. S. 865; (4) *American Hardware & Eq. Co.* v. *Commission of Int. R.,* 202 F. 2d 126 (C. A. 4), certiorari denied, 346 U. S. 814.

(1) *Textile Mills* has already been considered at length, pp. 24-25, 33-36, 44-46, *supra. Textile Mills* dealt with lobbying, which is not involved in the present case. *Textile Mills* did not deal with legitimate legislative activities directed against legislation that threatened destruction of the taxpayer's business, which is involved in the present case.

(2) *Sunset Scavenger* did not involve any inescapable destruction of business, and was moreover (84 F. 2d at 457) rested on the court's prior decision in *Old Mission P. Cement Co.* v. *Commissioner of Int. Rev.,* 69 F. 2d 676 (C. A. 9), affirmed on other issues, 293 U. S. 289, where the referendum for an increased gas tax levy to provide additional funds for road building (69 F. 2d at 677) bore only very remotely on the taxpayer's business, and where moreover the taint of lobbying was present; there the expenditure was listed on the taxpayer's books as "All California Highway Lobbying $3,000" (69 F. 2d at 681).

(3)(4) In both *Roberts Dairy* and *American Hardware* the expenditures took the form of contributions to the National Tax Equality Association, an organization which of course could not qualify within § 23 (q)(2) of the 1939 Internal Revenue Code, which dealt with the deduction of religious, charitable, scientific, educational and similar contributions by corporations. No question of the imminent destruction of an existing business was even remotely involved.

Consequently, even if knowledge of any of these decisions could be shown to have been brought home to the members of Congress who codified Section 23 (a)(1)(A) of the 1939 Code, or who participated in renumbering and recaptioning it in 1942 (Sec. 121(a) of the Revenue Act of [Oct 21,] 1942, c. 619, 56 Stat. 798, 819), it would not and could not have occurred to the most astute individual among them that, by taking such action with respect to a provision permitting the deduction of ordinary and necessary business expenses, he was simultaneously denying a taxpayer faced with legislation that threatened extinction of his business the right to deduct sums spent in openly opposing that legislation by means that did not involve lobbying.

In this connection, it must be borne in mind that the basic statute in the present case is Section 23 of the Code, "Deductions from gross income", and that the pertinent subsections are "(a) Expenses; (1) Trade or business expenses." The regulation now in question is Treas. Reg. 111, Sec. 29.23(o)-1, "Contributions or Gifts by Individuals", which is indexed under Sec. 23(o) of the Code, subsection (o) being "Charitable and other contributions."[20]

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[20] Contributions by corporations fall under subsection (q) of Section 23 of the Code, "Charitable and other contributions by

Subsections (a)(1) and (o) of Section 23 of the Code deal with entirely different matters. The first has to do with deductible business expenses, the second deals with deductible contributions by persons who do not have to be in business at all to obtain the deduction. Under Section 23(a)(1), an expenditure in order to be deductible must be incurred in carrying on a trade or business, and must additionally be ordinary and necessary; under Section 23(o)—and under Section 23(q)—there is no requirement that the contribution be an ordinary and necessary expense incurred in the course of operating a business.

Both Sections 23(o) and 23(q) limit the character of the recipients to whom a contribution when made is deductible; the donee must be an organization "no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation."

This proviso first appeared as a part of Sec. 23 (o)(2) in the Revenue Act of 1934, and as a part of what was added to that Act as Sec. 23(r) by § 102(c) of the Revenue Act of 1935. In the Revenue Act of 1936 the latter provision, relating to corporations, was renumbered Sec. 23(q).

When the proviso was first enacted, Congress was acutely aware of the existence of organizations whose primary purpose was the dissemination of propaganda under the guise of being charitable, religious, and educational in nature, and its objective was to deny deductibility to propagandist organizations. Amendment

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corporations." For present purposes, nothing turns on the distinction between individual and corporate taxpayers. Sections 23(o) and 23(q) of the 1939 Code are now combined as Section 170 of the 1954 Code.

No. 19, 78 Cong. Rec. 5861, 5959, 7816, 7821, 7831. It is on this basis that contributions to a political party are not deductible. Section 23(a)(1)(A) was not mentioned, for the obvious reason that the proviso as a part of Sec. 23(o), contributions, involved considerations wholly unrelated to Sec. 23(a)(1)(A), which dealt with business expenses. Section 23(o) dealt with the activities of the organization receiving money, Section 23(a)(1)(A) with the business activities of the person or organization spending money. And the portion of the regulation now in question (quoted at R. 136) was first inserted in 1938 as Treas. Reg. 101, Art. 23(o)-1, "Contributions or gifts by individuals."

In the *Textile Mills* case, the regulation relating to lobbying by corporations had a long history, see 314 U. S. at 337-338; the regulation was moreover supported by well recognized and established considerations of public policy; and the Court characterized as "frivolous" the taxpayer's contention that in those circumstances the regulation was inapplicable because indexed under a section of the act other than the one dealing with business expenses. We do not question the characterization as applied in those circumstances. But the issue under the present heading is not whether the regulation that is in question in the present case was applicable, it is not whether it would be valid as an original question, it is rather the very much more narrow inquiry as to whether this particular regulation can be deemed to have been reenacted by Congress.

It may be that the conscientious Congressman is as fictitious a character as the reasonable man. The standard both represent is real nonetheless. We ask, therefore, if a conscientious Congressman, faced with the bill that became the Internal Revenue Code of 1939, had sought to ascertain from the latest Treasury Reg-

ulations available, Treas. Reg. 101 of 1938, the meaning of "ordinary and necessary" business expenses in draft Section 23(a)(1), would he have looked to Art. 23(o)-1 of those regulations, entitled "Contributions or gifts to individuals", in order to find that meaning? And, if he had, would it ever have occurred to him that sums expended by a businessman in the course of legitimate activity designed to defeat legislation that would have destroyed his existing business were not deductible as ordinary and necessary business expenses by reason of the fact that contributions by taxpayers whether in business or not were not deductible when made to organizations that in substantial measure were engaged in opposing legislation?[21]

Unless both of these questions can be answered with a resounding affirmative—and of course neither can be—any talk of reenactment is just that—talk.

C. It is even more clear that there has been no reenactment of the regulation denying deductions for legislative expenses in its application to legislation enacted directly by the people without intervention of a legislature.

A fortiori, there has never been any regulation specifically mentioning expenditures made in respect of legislative measures submitted directly to the people by way of initiative, referendum, or constitutional amendment. In this field, even the prerequisite of

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[21] The regulation was numbered Sec. 23(o)-1, thus being indexed under the section of the Internal Revenue Code dealing with charitable contributions. As a glance at that regulation will show, the provision prohibiting expenses for lobbying and the promotion or defeat of legislation was buried in the midst of lengthy and detailed provisions dealing with charitable contributions. The same comment can be made regarding the regulation as it stood when the present controversy arose; see pp. 67-69, *infra*.

the reenactment doctrine—"regulations and interpretations long continued without substantial change" (*Helvering* v. *Winmill,* 305 U. S. 79, 83)—is lacking.

For, far from there being any long continued, consistent course of administrative holdings that the word "legislation" in the regulation includes measures enacted by direct vote of the people, the Tax Court held that a taxpayer could deduct as a business expense sums paid to further the adoption of a constitutional amendment—direct legislation by the people—which he believed would increase his business. *Luther Ely Smith,* 3 T. C. 696. Moreover, as has been seen, the Commissioner for fourteen long years publicly acquiesced in that holding.

That acquiescence, published in the light of the *Textile Mills* decision which preceeded *Luther Ely Smith* by more than two years, not only negatives any possible application of the enactment doctrine to support the ruling below, but actually requires reversal of the decision now under review by virtue of that precise doctrine.

Indeed, we submit that it is not open, even to the Government, to urge that its position is supported by reenactment on the footing of "regulations and interpretations long continued without substantial change," and simultaneously to put forward the Commissioner's delayed-action doctrinal somersault by way of additional argument.

It is plain that, under the present heading (Point III C), there is no scope for the reenactment doctrine. Only two rulings have been found—other than those now under review in this Court—where it was held that expenses incurred in connection with a referendum for the continuance or non-continuance of a busi-

ness dependent on periodic popular approval were non-deductible. *Revere Racing Association* v. *Scanlon*, 232 F. 2d 816 (C. A. 1) (dog racing); *Herbert Davis*, 26 T. C. 49 (liquor business). Both date from 1956, and so followed by many years the basic 1939 Act on which petitioners here rest their case. They are thus plainly insufficient to permit invocation of the doctrine of reenactment. For the rest, as this Court said (*Jones* v. *Liberty Glass Co.*, 332 U. S. 524, 534), "We do not expect Congress to make an affirmative move every time a lower court indulges in an erroneous interpretation."

Consequently, as we said in our Petition, any talk of "reenactment" in the present connection must be dismissed as sheerest fiction.

IV. Petitioners Sufficiently Proved That Passage of the Proposed Initiative Measure, Which Would Have Closed All Retail Stores for the Sale of Beer, Would Have Impaired Their Wholesale Business to the Point of Probable Destruction.

Little time need be spent on the alternative ground of affirmance espoused by the court below (R. 138-139), to the effect that petitioners failed to prove that the passage of the initiative measure here in question would have impaired their business to the point of probable destruction. Indeed, we cannot forbear the observation that, if there had been any substance to the alternative ground, this Court would scarcely have considered that the substantive questions presented by the Petition for Certiorari were in a posture that warranted review.

First. The only oral testimony in the record on the effect of the initiative came from Adwen, Secretary of the Washington Beer Wholesalers Association (R. 75), who testified (R. 76-77):

"A. Initiative 13 primarily would have in the opinion of the industry—I think I can safely say industry— would have made it necessary to distribute beer and wine through state liquor stores which would have automatically put the taverns and the grocery stores handling beer and wine out of business. At the same time it would undoubtedly have put at least 90 per cent of the beer wholesalers out of business. I don't say a 100 per cent for this reason. It would still probably be necessary for some of the breweries to have representatives to call upon the Liquor Board to sell their mechandise and their wares, but at least 90 per cent of them would have had nothing to do so they would have gone completely out of business."

In view of the terms of the initiative (R. 93-96), which would have given the State of Washington a monopoly of all beer retailing, which would have repealed all existing statutes relating to beer retailing, and which would have revoked all existing licenses to sell beer at retail, it is plain that petitioners—beer wholesalers—would have been forthwith deprived of all their existing customers. Yet despite the terms of the initiative, and despite Adwen's uncontradicted testimony, the district court found as a fact that (Fdg. 9, R. 46):

"9. There was testimony to the effect that the Initiative, if passed, would have affected the wholesale business of Cammarano Brothers. However, the way in which the measure, aimed as it was at retail sales of wine and beer, would have affected the wholesale distribution of beer was not made clear. In any event, the measure was defeated."

The court below, quoting the foregoing, called it (R. 139) "a finding that appellants failed to sustain

their burden of establishing by a preponderance of the evidence that the passage of the initiative would have impaired its business as a beer distributor."

Second. It is obvious from the foregoing that both courts have been thinking in terms of words rather than of actualities, and that by concentrating on the textual differences between the word "retail" and the word "wholesale", they both quite lost sight of the commercial nexus that links the two in the business world. In the context of trade the two imply a relationship, just as "buyer" and "seller", separate words, are joined in the transaction of sale.

The relationship between wholesale and retail is not obscure or mysterious; on the contrary, it is a commonplace of merchandising. "Wholesale" by dictionary definition is "the sale of commodities in large quantities, as to retailers or jobbers rather than to consumers directly (opposed to *retail*)." *The American College Dictionary* (Barnhart ed. 1947) 1393. "It is the character of sales to the trade that makes and distinguishes a wholesaler." *L. & C. Mayers Co.* v. *Federal Trade Commission,* 97 F. 2d 365, 366-367 (C. A. 2); see also *Roland Co.* v. *Walling,* 326 U. S. 657, 673-74.[22]

A wholesaler, accordingly, is one who sells to retailers. He can lose his business in one of two ways, either by having his own establishment closed or by having his customers' establishments closed. Either act effectively terminates his business. Obviously, when retail stores are closed, wholesalers have lost their trade for want of customers, and in this instance 90% of the wholesalers would have been out of busi-

[22] Sometimes, of course, "wholesaler" is more narrowly defined (*e.g.*, 26 U. S. C. §§ 4731(d), 5112), but such formulations are irrelevant in the present context.

ness. And under the terms of the initiative (R. 93-96) they could not have transformed their business from wholesaling to retailing, because that provided for all beer retailing to be done by the State of Washington.

All the above is really so pikestaff plain that it is within the realm of judicial notice, for what has just been said is a part of "the general customs and usages of merchants" (*Brown* v. *Piper,* 91 U. S. 37, 42) that will be so noticed, and is moreover quite as obvious as the proposition involved in the cited case, *viz.,* that a freezer which can freeze ice cream can likewise freeze fish.

The alternative holding of the court below, once it is subjected to just a moment's thought becomes—and is—utterly untenable.

Third. But if more technical grounds are necessary, they can easily be supplied; Finding 9 of the district court (R. 46), on which the court of appeals relied (R. 138-139), is doubly deficient by accepted standards of judicial administration.

1. In view of the Adwen testimony, quoted above at p. 60, and of the terms of the initiative (R. 93-96), Finding 9 is "clearly erroneous" within Rule 52(b), F. R. Civ. P., under the standard of *United States* v. *United States Gypsum Co.,* 333 U. S. 364, 395: "A finding is 'clearly erroneous' when although there is evidence to support it, the reviewing court on the entire evidence is left with the definite and firm conviction that a mistake has been committed." Here, of course, there was no evidence contradicting or even qualifying Adwen's testimony or the scope of the initiative provisions in any way.

2. The doctrine of judicial admissions similarly impairs Finding 9.

On the day of the trial, the Government filed a trial memorandum with the district court that stated in part (R. 18), "Concededly, Initiative 13 would have affected a portion of plaintiffs' business, and perhaps would have put them out of business entirely." In his opening statement, Government counsel sought to qualify or withdraw this concession (R. 73-74). But the law is that a judicial admission, once made, can only be withdrawn on a showing that what was admitted could not in any circumstance be true. See *L. P. Larson, Jr., Co.* v. *Wm. Wrigley, Jr., Co.*, 253 Fed. 914, 917-918 (C. A. 7), certiorari denied, 248 U. S. 580; *Oscanyan* v. *Arms Co.*, 103 U. S. 261, 263-264; 9 Wigmore, *Evidence* (3d ed. 1940) §§ 2588, 2590, 2591. No such showing, plainly enough, can be made; and certainly no such showing was attempted to be made.

Fourth. In this Court, it was for the first time urged that the deficiency in proof lies in the circumstance that petitioners did not show that they would have been among the 90% of the wholesalers who would have gone completely out of business according to Adwen's testimony. The Government said, referring to that testimony (Br. Op. 10-11), "This general statement, however, falls far short of demonstrating that the taxpayers themselves would have suffered, particularly in view of the same witness' admission (R. 76-77) [quoted *supra*, p. 60] that some of the wholesale distributors would still be required to have representatives call upon the State Liquor Board to sell their merchandise."

But the short answer to the foregoing is that a taxpayer who incurs expenses in attempting to save his business from destruction is not required to prove to a mathematical certainty that this would have hap-

pened. It is sufficient that the business was "threatened with complete destruction", *Commissioner* v. *Heininger,* 320 U. S. at 472, and that the expenditures made "are the common and accepted means of defense against attack." *Welch* v. *Helvering,* 290 U. S. at 114. Not only is the Government's newly generated position, that total destruction must be proved for a taxpayer to avail himself of the *Heininger* doctrine, without support in reason, it is also contrary to the authorities as to the deductibility of legal expenses incurred in defending criminal prosecutions and suits seeking penalties. There, as we have seen, *supra* pp. 22-23, the present case law is that such expenses are deductible if the defendant prevails but not if he loses.

Otherwise stated, the weaker the Government's case and the less the possibility of losing one's livelihood in consequence of prosecution, the greater the chance of deducting the expenses incurred in defending. Yet here the Government now seeks to rest non-deductibility on the fact that on the evidence there was only a 90 rather than a 100 per cent chance of petitioners being put out of business.

It is not necessary to labor the point. We submit that in the context of the statute, it is just as ordinary, and just as necessary, to avert a 90% possibility of the destruction of an income-producing enterprise as it is to avoid a 100% certainty of such destruction.[23]

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[23] The same reasoning disposes of the last sentence of Finding 9 (R. 46), "In any event, the measure was defeated." Under the cases dealing with the deductibility of expenses incurred in defending criminal prosecutions, success for the defendant makes an *a fortiori* case for deductibility and not the contrary, as the quoted sentence appears to imply.

Fifth. Finally, the Government says (Br. Op. 11), "The initiative measure, it should be noted, was not a prohibition measure, but only a measure designed to have beer and wine sold through state-owned stores." The relevance of that observation is not perceived; the question here is simply as to the effect of the initiative on petitioners' business. Since, plainly, it had a 90% chance of closing that business, its scope or lack of scope beyond that is obviously without bearing here.

CONCLUSION

For the foregoing reasons, the judgment below should be reversed, and the cause remanded with directions to enter judgment for the petitioners in the amount prayed for.

Respectfully submitted.

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APPENDIX

Statute, Regulation, and State Constitutional Provision Involved

1. Section 23(a)(1)(A) of the Internal Revenue Code of 1939 provides in pertinent part as follows:

> "§ 23. Deductions from gross income. In computing net income there shall be allowed as deductions:
>
> "(a) Expenses.
>
> "(1) Trade or Business Expenses.
>
> "(A) In General. All the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, * * *."

2. Section 29.23(o)-1 of Treasury Regulations 111, as it existed during 1948, was as follows:

> "Sec. 29.23(o)-1. Contributions or Gifts by Individuals.—
>
> "A deduction is allowable under section 23(o) only with respect to contributions or gifts which are actually paid during the taxable year, regardless of when pledged and regardless of the method of accounting employed by the taxpayer in keeping his books and records. A deduction is not allowable, however, for the actual payment of a contribution or gift if the amount of such payment already has been deducted on the accrual basis in computing net income for any taxable year beginning before January 1, 1938. A contribution or gift to an organization described in section 23(o) is deductible even though some portion of the funds of such organization is or may be used in foreign countries for charitable and educational purposes. This section does not apply to contributions or gifts by estates and trusts (see section 162). For computation of deductions for charitable contributions where the taxpayer also has an allowable deduction for medical expenses, see section 29.23(x)-1.
>
> "A contribution or gift to the United States, any State, Territory, or any political subdivision thereof, or the District of Columbia, or any possession of the United States exclusively for public purposes, is deductible.

"No reduction is allowed in computing the net income of a common trust fund or a partnership for contributions or gifts made to organizations described in section 23(o). (See sections 169 and 183.) However, a partner's proportionate share of contributions or gifts actually paid by a partnership during its taxable year to such organizations may be allowed as a deduction in his individual personal return for his taxable year with or within which the taxable year of the partnership ends, to an amount which, when added to the amount of contributions made by the partner individually and claimed as a deduction, is not in excess of 15 percent of his adjusted gross income, or, for taxable years beginning prior to January 1, 1944, 15 percent of his net income computed without the benefit of the deduction for contributions. In the case of a nonresident alien individual or a citizen of the United States entitled to the benefits of section 251, see sections 213(c) and 251. For contributions or gifts by corporations, see section 29.23(q)-1.

"In the case of husband and wife making a joint return, the deduction for contributions or gifts is the aggregate of such contributions or gifts made by the spouses, and is limited to 15 percent of the aggregate adjusted gross income of the spouses or, for taxable years beginning prior to January 1, 1944, 15 percent of the aggregate net income of the spouses computed without the benefit of the deductions for contributions.

"A donation made by an individual to an organization other than one referred to in section 23(o) which bears a direct relationship to his business and is made with a reasonable expectation of a financial return commensurate with the amount of the donation may constitute an allowable deduction as business expense.

"Sums of money expended for lobbying purposes, the promotion or defeat of legislation, the exploitation of propaganda, including advertising other than trade advertising, and contributions for campaign expenses, are not deductible from gross income.

"If the contribution or gift is other than money, the basis for calculation of the amount thereof shall be the fair market value of the property at the time of the contribution or gift.

"In connection with claims for deductions under section 23(o), there shall be stated in return of income the name and address of each organization to which a contribution or gift was made and the amount and the approximate date of the actual payment of the contribution or gift in each case. Claims for deductions under section 23(o) must be substantiated, when required by the Commissioner, by a statement from the organization to which the contribution or gift was made showing whether the organization is a domestic organization, the name and address of the contributor or donor, the amount of the contribution or gift and the date of the actual payment thereof, and by such other information as the Commissioner may deem necessary."

3. Amendment 7 to the Constitution of the State of Washington, adopted in November 1912, provides in pertinent part as follows:

"Art. 2 § 1. LEGISLATIVE POWERS, WHERE VESTED. The legislative authority of the state of Washington shall be vested in the legislature, consisting of a senate and house of representatives, which shall be called the legislature of the State of Washington, but the people reserve to themselves the power to propose bills, laws, and to enact or reject the same at the polls, independent of the legislature, and also reserve power, at their own option, to approve or reject at the polls any act, item, section or part of any bill, act or law passed by the legislature.

"(a) Initiative: The first power reserved by the people is the initiative. Ten per centum, but in no case more than fifty thousand, of the legal voters shall be required to propose any measure by such petition, and every such petition shall include the full text of the measure so proposed. Initiative petitions shall be filed with the secretary of state not less than four months before the election at which they are to be voted upon, or not less than ten days before any regular session of the legislature. If filed at least four months before the election at which they are to be voted upon, he shall submit the same to the vote of the people at the said election. If such petitions are

filed not less than ten days before any regular session of the legislature, he shall transmit the same to the legislature as soon as it convenes and organizes. Such initiative measure shall take precedence over all other measures in the legislature except appropriation bills and shall be either enacted or rejected without change or amendment by the legislature before the end of such regular session. If any such initiative measure shall be enacted by the legislature it shall be subject to the referendum petition, or it may be enacted and referred by the legislature to the people for approval or rejection at the next regular election. If it is rejected or if no action is taken upon it by the legislature before the end of such regular session, the secretary of state shall submit it to the people for approval or rejection at the next ensuing regular general election. The legislature may reject any measure so proposed by initiative petition and propose a different one dealing with the same subject, and in such event both measures shall be submitted by the secretary of state to the people for approval or rejection at the next ensuing regular general election. When conflicting measures are submitted to the people the ballots shall be so printed that a voter can express separately by making one cross (X) for each, two preferences, first, as between either measure and neither, and secondly, as between one and the other. If the majority of those voting on the first issue is for neither, both fail, but in that case, the votes on the second issue shall nevertheless be carefully counted and made public. If a majority voting on the first issue is for either, then the measure receiving a majority of the votes on the second issue shall be law."